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No. 02-1168

IN THE
Supreme Court of the United States

AMERICAN GENERAL LIFE INSURANCE COMPANY,

Petitioner,

v.

SPHERE DRAKE INSURANCE LIMITED,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

REPLY BRIEF

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STATEMENT PURSUANT TO RULE 29.6

Petitioner American General Life Insurance Company Rule 29.6 Statement was set forth at page (iii) of the Petition, and there are no amendments to that Statement.

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INTRODUCTION

Section 10 of the Federal Arbitration Act ("FAA") authorizes a district court to vacate an arbitration award where there was "evident partiality or corruption in the arbitrators, *or either of them*." 9 U.S.C. § 10(a)(2) (emphasis added). In the present case, the district court found that the intentional failure of Sphere Drake's party-appointed arbitrator to disclose his significant prior attorney-client relationship with Sphere Drake demonstrated evident partiality. The fact that there was a non-trivial business relationship between Sphere Drake's party arbitrator and Sphere Drake *combined* with the fact that the arbitrator purposefully concealed that relationship amply supports the district court's finding of evident partiality under § 10(a)(2).

The Seventh Circuit circumvents the disclosure rule announced in *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145 (1968), by reasoning that party-appointed arbitrators are mere shills, exempt from any disclosure obligation and free to exhibit evident partiality. Such a distorted interpretation is not supported by § 10(a)(2), which by its plain language prohibits evident partiality in both party-appointed arbitrators and "neutral" arbitrators. Moreover, *Commonwealth Coatings* and its progeny leave no doubt that the requirement to disclose any non-trivial relationship applies to all members of a tripartite arbitration panel. Finally, the parties here expressly intended the party-appointed arbitrators to be more than mere pitchmen. At the outset of the proceedings, the parties explicitly agreed that all members of the panel should disclose any prior relationships with the parties and their law firms. Such disclosure benefited not only the parties, but also the neutral arbitrator, who needed to assess any potential bias on the part of his fellow arbitrators. The Seventh Circuit's decision exempting the party arbitrators from § 10(a)(2) cannot be squared with its finding that the parties intended that the party arbitrators be "impartial adjudicators." Pet. App. 5a.

This case is an appropriate vehicle for this Court to reaffirm that the prophylactic disclosure rule announced in *Commonwealth Coatings* applies to all arbitrators, whether party-appointed or neutral. Reaffirming the need for full and candid disclosure by all arbitrators will help promote arbitration as a legitimate and desirable alternative to litigation. The Seventh Circuit's decision sanctioning evident partiality on the part of an "impartial adjudicator" impugns the integrity of the arbitral process and should not be allowed to stand.

ARGUMENT

POINT I

SPHERE DRAKE IGNORES THE PLAIN LANGUAGE OF § 10(a)(2)

Sphere Drake argues that All American's petition "proceeds entirely on the premise that a failure of 'disclosure' constitutes" a violation of § 10(a)(2)'s evident partiality standard. Br. in Opp. 11-12. Sphere Drake's characterization of All American's argument is wrong. This case is not one in which a party-appointed arbitrator simply failed to disclose a prior non-trivial relationship with the appointing party. Sphere Drake's party arbitrator deceived All American and the other arbitrators by failing to disclose his significant prior attorney-client relationship at the outset of the proceedings, thereby demonstrating his evident partiality.

The Seventh Circuit held that the statutory ground for vacating an arbitration award under § 10(a)(2) of the FAA does not extend to party-appointed arbitrators. As demonstrated in All American's Petition, the Seventh Circuit's holding is inconsistent with the plain language of § 10(a)(2), which authorizes a district court to vacate an award where there was "evident partiality or corruption in the arbitrators, *or either of them*." *See* Pet. 10 (emphasis added). The italicized words leave no room to dispute the intent of Congress to include party arbitrators on a tripartite panel.

Sphere Drake attempts to rehabilitate the Seventh Circuit's unprecedented decision by arguing that the plain language of § 10(a)(2) should be construed "in light of the parties' specific agreement to arbitrate." Br. in Opp. 13. According to Sphere Drake, because the parties appointed their arbitrators, All American could not expect them to be "neutral" or "impartial," presumably meaning there was an intent to exempt them from the prohibition of § 10(a)(2) against evident partiality. Sphere Drake's argument is without factual or legal support.

First, the parties held an organizational meeting at which each panel member made a disclosure concerning his current and past relationships with the parties, their respective law firms and the other panel members in accordance with the procedure agreed to among the panel and counsel. Logically, the parties would not have bothered to go through the process of soliciting disclosures from the party-appointed arbitrators unless the parties believed those disclosures would be meaningful, *i.e.*, would provide a basis for assessing potential bias or evident partiality.

Second, disclosure by Sphere Drake's party-appointed arbitrator served a number of salutary purposes. Had Sphere Drake's party arbitrator disclosed the truth about his extensive attorney-client relationship with Sphere Drake, All American would have had a meaningful opportunity to exercise its right to challenge his appointment. *See Metropolitan Prop. & Cas. Ins. Co. v. J.C. Penney Cas. Ins. Co.*, 780 F. Supp. 885, 894 (D. Conn. 1991) (a party-appointed arbitrator can be disqualified prior to arbitration); *Lipschutz v. Gutwirth*, 304 N.Y. 58, 65 (N.Y. 1952) (same). Moreover, such disclosure would have provided the umpire with information necessary to assess the appropriate weight to be given to the party-appointed arbitrator's views. Commentators recognize the importance of such disclosure: "[w]hat the neutral learns about the party arbitrators' relationships with their parties should also be useful to him in evaluating the points those arbitrators make to him about the case." Stephen C. Rogers, *Can Tripartite Arbitration Panels*

Reach Fair Results?, 8 No. 1 Disp. Resol. Mag. 27, 29 (Fall 2001). *See also* the Revised Uniform Arbitration Act § 12, Comment 5:

> The integrity of the process demands that the non-neutral arbitrators chosen by the parties, like neutral arbitrators, disclose pertinent interests and relationships to all parties as well as other members of the arbitration panel. *It is particularly important for the neutral arbitrator to know the interest of the arbitrator selected by each of the parties if, for example, such non-neutral arbitrator is being paid on a contingent-fee basis.*

Emphasis added.

Finally, strict disclosure standards are a necessary check on the significant power exercised by arbitrators. The Seventh Circuit was wrong to hold that arbitrators should be held to a less stringent disclosure standard than judges. Instead, as this Court recognized in *Commonwealth Coatings*, "we should, if anything, be even more scrupulous to safeguard the impartiality of arbitrators than judges, since the former have completely free rein to decide the law as well as the facts and are not subject to appellate review." 393 U.S. at 149. Rigorous disclosure standards are also necessary for arbitrators because, as the Seventh Circuit acknowledged, industry arbitration "often uses panels composed of industry insiders, the better to understand the trade's norms of doing business and the consequences of proposed lines of decision." App. at 4a. This reality demands that the parties and other arbitrators be cognizant of the extent of an arbitrator's relationship to the party that selected him or her, which can only be achieved through the full and candid disclosure by all arbitrators, as required by this Court in *Commonwealth Coatings*.

POINT II

THE SEVENTH CIRCUIT'S DECISION IS CONTRARY TO *COMMONWEALTH COATINGS*

The Seventh Circuit held here that the disclosure requirement set forth in *Commonwealth Coatings* applies only to a neutral arbitrator in a tripartite arbitration, and not to party-appointed arbitrators. This holding is unsupportable. *Commonwealth Coatings*, which involved precisely the same type of tripartite panel as the present case, draws no distinction between the disclosure obligations of neutral and party-appointed arbitrators. *See Commonwealth Coatings*, 393 U.S. at 151-52 (White, J., concurring) (encouraging an "atmosphere of frankness at the outset," which could not be achieved where only one of three arbitrators on a tripartite panel is required to disclose his or her prior relationships); *id.* at 149 (Black, J., concurring) ("[w]e can perceive no way in which the effectiveness of the arbitration process will be hampered by the simple requirement that *arbitrators* disclose to the parties any dealings that might create an impression of possible bias") (emphasis added). *See also Standard Tankers (Bahamas) Company, Ltd. v. Motor Tank Vessel, Akti*, 438 F. Supp. 153, 159 (E.D.N.C. 1977) (*Commonwealth Coatings* "placed a disclosure burden on arbitrators appointed by the parties or otherwise."); Pet. 10-15 (authorities cited therein).

Sphere Drake attempts to shore up the Seventh Circuit's holding by suggesting that *Commonwealth Coatings* is in fact a disqualification case, rather than a disclosure case. Br. in Opp. 18 (stating that, in *Commonwealth Coatings*, the Justices "focused" on whether an arbitrator would be disqualified by a business relationship with the parties). Having thus misinterpreted the holding of *Commonwealth Coatings*, Sphere Drake explains that the true issue in the present case is whether or not Sphere Drake's party arbitrator had an "ongoing pecuniary interest" in the outcome of the arbitration. *Id.* This is wrong. *Commonwealth Coatings*, which represents the seminal case

concerning an arbitrator's — any arbitrator's — duty to disclose, holds that the failure of an arbitrator to disclose a non-trivial business relationship with a party constitutes evident partiality under the FAA, regardless of whether the arbitrator had an "ongoing pecuniary interest." Indeed, in *Commonwealth Coatings*, there had been no dealings between the arbitrator in question and the respondent for "*about a year* immediately preceding the arbitration." 393 U.S. at 146 (emphasis added).

Applying the *Commonwealth Coatings* holding to the present case, the district court found that Sphere Drake's arbitrator was evidently partial due to his failure to disclose a significant four-year attorney-client relationship with Sphere Drake, a relationship misleadingly described by the arbitrator as simply providing "limited corporate advice." All American has never argued, contrary to Sphere Drake's suggestion, that the party arbitrator's nondisclosure itself constitutes an "independent" ground for vacating the award. Br. in Opp. 19. Rather, All American argued, and the district court agreed, that given the totality of the circumstances, the arbitrator's "troublesome" and "disappointing" failure to disclose his "substantial" relationship with Sphere Drake was sufficient to establish evident partiality under § 10(a)(2). Pet. App. 27a; 13a. Importantly, the Seventh Circuit did not disagree with this finding. Instead, the Seventh Circuit wrongly held that Sphere Drake's party arbitrator was exempt from § 10(a)(2) and any duty to disclose, and thus *Commonwealth Coatings* did not apply.

Sphere Drake erroneously argues that a failure to disclose is never sufficient to establish evident partiality. Br. in Opp. 19. However, the very case to which respondent cites in support of this position, *ANR Coal Company, Inc. v. Cogentrix of N. Carolina, Inc.*, 173 F.3d 493, 500 (4th Cir. 1999), itself holds that "an arbitrator's failure to reveal facts may be relevant in determining evident partiality under 9 U.S.C. § 10(a)(2)." The fact that the court in *ANR Coal* held that the failure of a neutral arbitrator to disclose prior representation by his law firm

of a party, *with which the arbitrator had no personal involvement*, did not demonstrate evident partiality is irrelevant; here, the trial court found that the arbitrator's failure to disclose his own substantial attorney-client relationship with Sphere Drake did constitute evident partiality.

Finally, All American does not concede, as alleged by Sphere Drake, that the undisclosed information about the arbitrator's prior relationship would not have, if disclosed, required disqualification. Br. in Opp. 19. All American has not taken any position on that question because it is simply not relevant to this case.[1] The arbitrator's intentional concealment of his prior, non-trivial relationship is an integral part of the fact pattern; it cannot be ignored in an effort to change the issue in this case from evident partiality to disqualification.

The Supreme Court Rules explicitly provide that a grant of certiorari is appropriate where "a state court or a United States court of appeals . . . *has decided an important federal question in a way that conflicts with relevant decisions of this Court.*" Sup. Ct. R. 10 (emphasis added). Here, the Seventh Circuit has disregarded this Court's ruling in *Commonwealth Coatings* that all arbitrators must disclose any non-trivial business relationship with a party to the arbitration under § 10(a)(2). Such a blatant departure from this Court's prior holding demands the Court's review. Thus, respondent's contention that a grant of certiorari is not warranted because there is no circuit split is simply irrelevant.

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1. Throughout its brief, Sphere Drake contends that All American "concedes" that the prior relationship, if disclosed, would not have required disqualification or demonstrated evident partiality. Br. in Opp. 11, 19 (citing to Pet. 13). All American has made no such concession. Sphere Drake misconstrues All American's Petition, which states merely that the Seventh Circuit's misguided interpretation of *Commonwealth Coatings* "stems, at least in part from the court's implicit finding that disclosure by a party arbitrator serves no salutary purpose if the facts to be disclosed would not result in the arbitrator's disqualification." Pet. 13.

POINT III

ARBITRATION RULES AND POLICY ARGUMENTS UNDERMINE THE SEVENTH CIRCUIT'S DECISION

The Seventh Circuit's decision is broadly worded and, if permitted to stand, will be used to excuse (and indeed encourage) the practice of misleading disclosures by party-appointed arbitrators in a variety of circumstances. Hence, respondent is incorrect to argue that All American's reliance upon arbitration rules and policy arguments is "misplaced and without merit." Br. in Opp. 23-27. In fact, arbitration rules and policy arguments vividly illustrate the negative impact the Seventh Circuit's decision will have on the integrity of the arbitration process.

First, the Seventh Circuit operated under the assumption that the ARIAS-U.S. rules were employed, and thus its decision must be read as applicable to any case where those rules, or similar rules, are in effect. Pet. 16, 19 (finding that the "arbitration was conducted under the auspices of . . . ARIAS-US" and that according to the relevant rules, the party-appointed arbitrators are supposed to be "impartial adjudicators."). Having determined that Sphere Drake's party arbitrator was expected to be an *impartial adjudicator*, the Seventh Circuit nevertheless held that he had no disclosure obligation. Thus, the court's holding eviscerates any disclosure obligation for a party-appointed arbitrator regardless of the parties' expectation that the party arbitrators would be impartial and provide full disclosure, even where the applicable rules *require* disclosure. This decision squarely conflicts with the intended purpose of the disclosure rules adopted by various arbitration institutions, including the American Bar Association Revised Code of Ethics. *See Code of Ethics for Arbitrators in Commercial Disputes (Proposed Revision 2000)*, 671 PLI/Lit 1039, * 1056 (March 2002).

Second, this Court has adopted a clear policy of encouraging parties to resolve their disputes through arbitration, rather than litigation. Pet. 19-22. Failing to require full and honest disclosure

from all arbitrators will frustrate this stated policy by undermining the public's confidence in arbitration as a fair and viable alternative to litigation. *See Barcon Assoc., Inc. v. Tri-County Asphalt Corp.*, 430 A.2d 214, 219-20 (N.J. 1981) ("[A] party-designated arbitrator . . . must remain faithful to the obligation which rests upon him to maintain 'broad public confidence in the integrity and fairness of the (arbitration) process.'") (citing to the First Code of Ethics for Arbitrators in Commercial Disputes jointly drafted by the American Arbitration Association and the American Bar Association); *Metropolitan Prop. & Cas. Ins. Co. v. J.C. Penney Cas. Ins. Co.*, 780 F. Supp. 885, 893 (D. Conn. 1991) ("even a party-appointed arbitrator in the tripartite context 'has a responsibility not only to the parties but also to the process itself, and must observe high standards of conduct so that the integrity and fairness of the process will be preserved.'").

POINT IV

THIS CASE IS AN APPROPRIATE VEHICLE FOR REAFFIRMING *COMMONWEALTH COATINGS*

Sphere Drake's argument that this case is an inappropriate vehicle for Supreme Court review because the arbitral procedure was *ad hoc* is a red herring aimed at diverting the Court's attention from the real issue. Whether the arbitral procedure was *ad hoc* or institutional is irrelevant. Both types of arbitrations are governed by the FAA. The issue is whether Sphere Drake's party-appointed arbitrator was evidently partial in violation § 10(a)(2) of the FAA.

Further, Sphere Drake argues that this case is not ripe for certiorari review because the Seventh Circuit remanded the case for further proceedings in the district court. However, it is black letter law that this Court is not constrained by the final judgment rule. *See* 28 U.S.C.A. § 1254(1) (the Court may review cases by "writ of certiorari granted upon the petition of any party to any civil or criminal case, before or after rendition of judgment or decree."). Indeed, in *Forsyth v. Hammond*, 166 U.S. 506,

513 (1897), this Court referred to certiorari as "a comprehensive and unlimited power" that may be utilized "irrespective of any ruling or determination" of the court of appeals. This Court has exercised its jurisdiction in a wide range of cases requiring further action below. *See, e.g.*, *School Bd. of Nassau Cty., Fla. v. Airline*, 480 U.S. 273 (1987) (granting review after court of appeals reversed district court's dismissal and remanded for further proceedings); *INS v. Cardoza-Fonseca*, 480 U.S. 421 (1987) (granting review after court of appeals remanded case to Board of Immigration Appeals for further proceedings); *Stafford v. Briggs*, 444 U.S. 527 (1980) (granting review after court of appeals issued order upholding personal jurisdiction and remanding to district court for trial); *accord* C. Wright & A. Miller, 17 Fed. Prac. & Proc. Juris. 2d § 4036, at 3 ("In a wide range of cases, certiorari has been granted after a court of appeals has disposed of an appeal from a final judgment on terms that require further action in the district court, so that there is no longer any final judgment."). This case is ripe for review.

CONCLUSION

Petitioner respectfully submits that the Court should grant a writ of certiorari to reaffirm that the disclosure rule announced in *Commonwealth Coatings* applies to all arbitrators, neutral and party-appointed.

Respectfully submitted,

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